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No. 88-446

In the Supreme Court of the United States

OCTOBER TERM, 1988

CONTEMPORARY MISSION, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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Petitioner contends that the courts below erred in finding that it did not satisfy the statutory qualifications for tax exemption under Section 501(c)(3) of the Internal Revenue Code of 1954.[1]

1. Petitioner is an organization comprising a small group of Catholic priests whose avowed purpose is to promote a "communications and self-improvement apostolate." Petitioner has five members. They met in 1967 while studying at the Montfort Fathers seminary in St. Louis and did inner-city work together there in the late 1960's. As a result of differences with the Montfort Fathers, the group broke away in the early 1970's and moved east to Westport, Connecticut. Petitioner purchased a 19-room mansion with a swimming pool on two acres of waterfront property overlooking Long Island Sound. All of the group resided there, as well as the wife and children of one

[1] Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended (the Code).

member.[2] Pet. App. 5a-11a; C.A. App. A939, A942.

Petitioner did not solicit donations and received few, if any.[3] Instead, petitioner sold products through the mail, an activity which it claimed promoted its "communications and self-improvement apostolate." During the late 1960's and early 1970's, petitioner sold record albums and pamphlets claimed to be of a spiritual self-improvement nature which its members recorded or wrote. By 1977 however, petitioner no longer sold those items. Instead, petitioner sold tax guides guaranteed to save taxpayers a minimum of $500, diet books, weight-reducing bath salts, exercise devices, jewelry with "mood stones," books on golf, and a book containing Edgar Cayce's secrets to youth, beauty and health. None of these items was produced by petitioner. Instead, it purchased the right to market them from outside sources. Pet. App. 8a-18a.

In 1977, petitioner grossed more than $1,460,000 from sales of these items, with sales of the Edgar Cayce book and the tax guides each exceeding $400,000.[4] In that year

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[2] Although it was stipulated that each member was ordained in the Roman Catholic Church and authorized to administer its sacraments, member O'Reilly married in 1975 and fathered four children (Pet. App. 10a-11a; C.A. App. A556).

[3] O'Reilly testified that his mother gave him money to finance a Mercedes 450 XL. There was no other evidence that petitioner received any donations (C.A. App. A946).

[4] O'Reilly admitted that the tax guides were "not * * * religious book[s] as such" but claimed that they were part of petitioner's "self-improvement apostolate" (C.A. App. A641-A642).

In 1978 and later, Berkery, petitioner's leader, wrote four books which petitioner sold, along with other items, through the mail—*Relaxation Diet Program* (a "diet program based on meditation"), *The Secret* ("a self-fulfillment program which tries to teach a person how to better himself totally"), *Edgar Cayce Guide to Self-Healing* and *Biofeedback Without Machines* (both dealing "with self-

it realized a net profit of more than $250,300 from the mail order operation. Pet. App. 14a, 17a. Its members, as a group, devoted approximately ten percent of their working time to the mail order operation, with O'Reilly working five to six hours a day coordinating the entire enterprise. Although almost every member worked on the operation at one time or another, the petitioner also contracted for independent organizations to do much of the work and paid O'Reilly's wife and other outsiders to assist on jobs performed "in-house." C.A. App. A632, A640.

Petitioner prepared its own solicitation materials and hired printers to print the materials and envelopes. It rented mailing lists from commercial list brokers that targeted likely buyers and directed its promotions to individuals shown on those lists. In 1977, petitioner, using other organizations to do the mailing, sent approximately 12 million solicitations throughout the United States, with the bulk of those (more than 9 million) being for the tax guides. It used fictitious names when advertising, *e.g.*, "C.M., Inc., Tax Research Center" and "Golf Research Center," believing that this would increase its sales, and it test-marketed items to determine how profitable they might be. Pet. App. 14a-18a.

Proceeds from the direct mail operation were deposited in petitioner's checking accounts and, through transfers, drawn upon by its members. In 1977, petitioner spent more than $200,500 of the approximately $250,300 net profits realized from the operation on its members and their families. Petitioner did not pay its members a salary, as such, but provided each member with his every need, as well as many luxuries such as frequent restaurant meals, musical instruments (including a Steinway piano), exercise

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fulfillment"). Berkery viewed these books as part of his "religious communication apostolate" (Pet. App. 9a; C.A. App. A999-A1001).

classes, and seminars at self-improvement schools such as EST and the Option Method Institute. Shelter was provided in the 19-room mansion on Long Island Sound. Transportation was provided by making cars (three Mercedes) and a motorcycle available for use. Petitioner also provided the group with a yacht kept docked outside its house. Under the general supervision of either O'Reilly or Berkery, each member had authority to write checks on petitioner's accounts and each did so, sometimes for thousands of dollars at a time. Although large sums of cash were involved, no records were maintained showing their disposition. At trial, the members were unable to explain the specific purpose for many expenditures and offered incompiete, vague, and sometimes overlapping explanations for them. Pet. App. 18a-23a; C.A. App. A946-A947.

2. In 1970, petitioner sought a determination as to its exempt status under Section 501(c)(3) of the Code, submitting a statement by a vice-rector of the Missionary Society of the Holy Apostles that petitioner was "affiliated" with that Society and that once the association was "finalized," petitioner would be included under the Society's "banner" in the Official Catholic Directory. Based on that statement, the District Director of Internal Revenue issued an advisory letter stating that inasmuch as petitioner was an "integral part" of the operation of the Society, which was itself covered by the group exemption letter held by the U.S. Catholic Conference, petitioner also would qualify for exemption under that group letter. Pet. App. 6a-7a.[5]

Several years later, the District Director examined petitioner's operations and in a letter dated September 11, 1979, revoked his prior advisory letter effective as of

[5] A representative of the Missionary Society later advised the Service that the Society had, in fact, no relationship with petitioner, except a "spiritual association" (Pet. App. 7a).

January 1, 1977. The District Director found that petitioner was not exempt under the group ruling issued to the U.S. Catholic Conference since procedures for "obtaining or maintaining exemption as a subordinate organization affiliated with, and under the general supervision and control of" that Conference, had not been met.[6] He also found that petitioner did not qualify for exemption in its own right, because the evidence showed that it operated with a substantial commercial purpose and not exclusively for tax-exempt purposes as required by Section 501(c)(3). He found that petitioner also failed to show that no part of its net earnings inured to the benefit of private individuals and that it served public rather than private interests. Pet. App. 11a-13a; C.A. App. A50.

Petitioner sought review of the District Director's determination in the Claims Court pursuant to Section 7428 of the Code. After trial, that court sustained the District Director's position (Pet. App. 4a-32a). The court held that as of 1977, petitioner's primary goal in operating its mail order business was to generate commercial income, and that it engaged in that business on a substantial scale, both in an absolute sense and in relation to its other activities (*id.* at 23a-29a). The court also agreed that petitioner failed to show that no part of its net earnings inured to the benefit of private individuals. Petitioner's five members controlled petitioner, dictated when and for what purpose its revenue would be spent, and in fact spent almost all of it on themselves. The potential for abuse present under these circumstances required open and candid disclosure

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[6] Under those procedures, the Conference must "submit annually a list of organizations to be dropped or added to the group ruling," which it accomplishes "by submitting a copy of the Official Catholic Directory." Petitioner, the District Director noted, "does not, and has never, appeared in the Directory." C.A. App. A50.

of the facts and a full explanation of each expenditure made, yet the court pointed out that that had not been provided. It also found that the benefits received were patterned more to the members' individual needs and wants than to any measured contribution to the business, and could not be taken to represent payment of reasonable compensation by an organization operated for a public interest (*id.* at 29a-32a). The court of appeals affirmed, agreeing with the Claims Court that petitioner failed to qualify as a tax-exempt organization both because it was not operated primarily for tax-exempt purposes and because a substantial part of its net earnings inured to the member-priests and their families (*id.* at 1a-3a).

3. a. It is well established that the question whether an organization has a non-exempt purpose that is sufficiently substantial to make it ineligible for a Section 501(c)(3) tax exemption, rather than one that is merely incidental to its operations, is a question of fact. See, *e.g.*, *Church By Mail, Inc.* v. *Commissioner*, 765 F.2d 1387, 1390 (9th Cir. 1985); *Scripture Press Found.* v. *United States*, 285 F.2d 800 (Ct. Cl. 1961), cert. denied, 368 U.S. 985 (1962). Whether any part of an organization's net earnings inures to private persons is also a question of fact. See, *e.g.*, *Bubbling Well Church of Universal Love, Inc.* v. *Commissioner*, 670 F.2d 104 (9th Cir. 1981). The factual conclusions of both courts below that petitioner failed to qualify for a Section 501(c)(3) tax exemption on both of these grounds were amply supported by the record.

In particular, petitioner's sales of items such as tax guides, golf lessons, and exercise devices could hardly be viewed as furthering the communications apostolate that it allegedly sought to promote, and its members admitted as much. Yet in 1977, those non-religious products were virtually all it sold, a fact compelling the inference that its

primary goal in operating the business was the commerical one of making the largest profits possible. By the same token, the finding that petitioner engaged in the business on a substantial scale was supported by the facts showing that its members devoted significant time to the work while also subcontracting out much of it, that they conducted business on a grand scale sending out millions of solicitations and using the marketing techniques of a commercial mail order house, and that they netted over a quarter of a million dollars in profits in 1977 alone. Similarly, the inurement finding was supported by evidence showing that the members spent 80% of those profits on themselves, on items going well beyond mere subsistence.

b. Petitioner mainly argues (Pet. 8-14) that providing its members with subsistence should not be considered inurement and raising funds to pay for that should not destroy its exemption. At bottom, this is nothing more than an attack on the findings of fact below, and one entirely without merit.

To begin with, there is no support for the contention that the members received only subsistence. Petitioner spent more than $200,000 in 1977 alone (more than $40,000 per member) on that "subsistence." Rather than living in a frugal or ascetic fashion consistent with a vow of poverty, they enjoyed every manner of luxury. Petitioner's members exercised complete and unfettered control over petitioner and could use its earnings however they pleased. Thus, their failure to justify the generous benefits which they provided for themselves—and to explain the purpose for many other expenditures made—compelled an inference of impermissible inurement.

There is no basis for petitioner's suggestion (Pet. 8, 12-13) that it is no different from the religious order involved in *Trinidad* v. *Sagrada Orden*, 263 U.S. 578 (1924),

and that the decisions below are in conflict with that case.[7] In *Sagrada Orden* the parties stipulated that no part of the organization's net earnings inured to the benefit of any private individual (*id.* at 579-580). Also, in that case, unlike here, the organization clearly had no substantial non-exempt purpose. Most of its income was from investments, and the small profit made from sales of wine and other articles supplied for use in its churches could not destroy the exemption because the courts there found as a fact that "[f]inancial gain" was "not the end to which [those sales were] directed" (*id.* at 582). Here, to the contrary, the courts found that beginning in 1977, financial gain was the ultimate purpose for petitioner's operation of its mail order business. There is no reason for this Court to depart from its usual practice of declining to review the concurrent findings of fact of two lower courts. See, *e.g.*, *Berenyi* v. *Immigration Director,* 385 U.S. 630, 635-636 (1967).

c. Petitioner argues that denial of its tax exemption violates the Free Exercise and Establishment Clauses of the First Amendment because the courts applied "different and more rigorous" standards in testing its status than those applied to religious orders of the Roman Catholic Church (Pet. 15-17). It claims that although the government's position is that its members "spent too much time and money on their direct mail activity" and "did not adequately substantiate their religious activities," the Internal Revenue Service has approved similar direct mail activity

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[7] Petitioner's assertion (Pet. 10) that it is an "acknowledged religious order" again finds no support in the record. Although petitioner claimed to be a pious society of the Roman Catholic Church, it produced no documents to support that contention, has never been listed in the Official Catholic Directory, and is not included among the organizations covered by the group ruling issued to the U.S. Catholic Conference (Pet. App. 22a-23a).

in several private letter rulings issued to various Roman Catholic orders (*id.* at 15-16).[8] But it is clear that each taxpayer must establish its own qualification for exemption; a taxpayer cannot premise its right to an exemption on an assertion that others have been treated generously, leniently or erroneously by the Internal Revenue Service. See, *e.g., Dixon* v. *United States,* 381 U.S. 68 (1965); *Founding Church of Scientology* v. *United States,* 412 F.2d 1197, 1200 (Ct. Cl. 1969), cert. denied, 397 U.S. 1009 (1970). That the organizations covered by the rulings that petitioner has cited were able to demonstrate that they conduct a sufficiently large array of exempt activities to warrant a finding that the mail order activity of each was only incidental, and not animated by a substantial commercial purpose, is ultimately irrelevant to the question whether petitioner's mail order activities were a substantial part of its operations.

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[8] Petitioner claims (Pet. 17) that the courts below "refused to consider the priests' prayer and worship as part of their exempt activities." That is not correct. The record shows that the members described the nature, existence and performance of the activities that they claimed entitled it to exemption only in the most vague and general terms. Some described anecdotally some of their counseling activities, but they offered no records or other corroboration of such activities (C.A. App. A628-A629, A1014-A1015). In some instances they testified as to what a "typical" day consisted of. For example, Berkery testified that "typically" he would get up, pray and say mass, exercise, eat meals, and then, that he "might" spend some time socializing, meditating, writing, answering his mail, making phone calls, or counseling (C.A. App. A993-A997). In contrast, they testified at length and with specificity about the mail order business and the time and effort devoted to it. On the record, the lower courts certainly were warranted in finding that the mail order business was a substantial part of the overall operation and was animated by a substantial commercial purpose.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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